ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author:	Plescia	Analyst:	Kristina E. North	Bill Number:	AB 505
Related Bills:	See Legislative History	Telephone:	845-6978	Introduced Date:	February 20, 2007
		Attorney:	Daniel Biedler	Sponsor:	

SUBJECT: Qualified Vehicle Credit

SUMMARY

This bill would provide a tax credit for qualified vehicle costs.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to provide taxpayers with an additional incentive to purchase fuel-efficient, environmentally-friendly vehicles.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2007.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Current federal and state tax laws provide various tax credits designed to provide tax relief for taxpayers that incur certain expenses (e.g., child and dependent care credits) or to influence business practices and decisions or to achieve social goals.

Board Position:			Department Director	Date
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The federal Energy Policy Act of 2005 (EPACT) created a tax credit for individuals and businesses that buy or lease a new hybrid gas-electric car or truck after January 1, 2006. The credit ranges from $250 - $3,400, depending on the fuel economy and the weight of the vehicle. The credit will be phased out for each manufacturer when that company has sold 60,000 eligible vehicles. At that point, the tax credit for each company's vehicles will be gradually reduced over the course of another year. The following requirements must be met to claim the credit:

- The original use of the vehicle commences with the taxpayer,
- The vehicle is acquired for use or lease by the taxpayer, and not for resale,
- The vehicle is used mostly in the United States, and
- The vehicle must be placed in service by the taxpayer after December 31, 2005, and must be purchased on or before December 31, 2010.

Current state law lacks a deduction or tax credit for hybrid vehicles.

THIS BILL

This bill would provide a credit in the amount of an undetermined percentage of the aggregate amount paid for a qualified vehicle during a taxable year.

Qualified vehicle means a hybrid vehicle or alternative fuel vehicle that meets either of the following criteria:

- California's advanced technology partial zero-emission vehicle (AT PZEV) standard for criteria pollutant emissions, or
- California's ultra-low emission vehicle (ULEV), super ultra-low emission vehicle (SULEV), or partial zero-emission vehicle (PZEV) standards.

Unused credits can be carried over to future years until the credit has been exhausted.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

- The term "aggregate amount" is undefined and could include costs for unintended items such as tire replacement, fuel purchase, or other costs.
- This bill fails to limit the credit to a purchase or initial lease of a qualified vehicle and thus the credit could be available for any amount paid in connection with a vehicle that is purchased, leased, or rented, including extended warranties, sales or use tax, or service contracts.
- This bill fails to limit the credit to the year of purchase or use, so the credit could be available in later years for expenses such as registration fees and insurance.
- This bill fails to limit the credit to the first purchase or use, so the credit could be claimed several times as the vehicle is transferred, leased, or rented.

- This bill fails to limit the credit to end users/consumers and could include a credit for other taxpayers, such as car dealers, lessor, or rental companies. In addition, in the case of a lessor or rental company, the lessor or rental company could get the credit for the purchase of the vehicle and the lessee or renter could get also get a credit for the same vehicle for the percentage of the amounts paid during the year on their lease or rental.
- The percentage of the aggregate amount is unstated. The revenue impact is indeterminable without a stated percentage.
- The department lacks the expertise necessary to determine which vehicles would qualify for this credit. The author may wish to consider having a third-party, such as the Department of Motor Vehicles, certify which vehicles qualify for this credit.

LEGISLATIVE HISTORY

SB 308 (Margett, 2007/2008) is identical to AB 2616 (2005/2006). SB 308 is currently in the Senate Revenue and Taxation Committee where it may first be acted upon on or after March 22, 2007.

AB 2616 (Nakanashi, 2005/2006) would have provided to personal income taxpayers a $3,000 deduction for purchasing or leasing a hybrid vehicle. AB 2616 was held in the Assembly Revenue and Taxation Committee.

AB 838 (Saldana, 2005/2006) would have allowed individuals and businesses that purchase "qualified vehicles" a tax credit equal to the amount of the vehicle license fee paid annually to register one of these vehicles. AB 838 was held in the Assembly Appropriations Committee.

AB 1390 (Ridley-Thomas, 2003/2004) would have allowed a tax credit for the purchase of a new fuel-efficient vehicle if the Department of Finance certified that it found projected state revenues would exceed projected state expenditures. This bill remained in the house of origin.

AB 198 (Nation, 2003/2004), AB 848 (Nation, 2003/2004), and AB 2484 (Ridley-Thomas, 2003/2004), would have denied the general California business incentives relating to vehicles when a business purchased a large sport utility vehicle (SUV). The revenue from disallowing these incentives would have been used to fund a credit for the purchase and use of qualified reduced-emission vehicles in this state. AB 198 was held in Senate Appropriations; AB 848 and AB 2484 were held in Assembly Appropriations.

PROGRAM BACKGROUND

The California Air Resources Board (CARB) gathers air quality data for the State of California, ensures the quality of this data, designs and implements air models, and sets air quality standards for the state. CARB is part of the California Environmental Protection Agency, an organization that reports directly to the Governor.

Listed below are emission ratings established by CARB:

1. Low-Emission Vehicle (LEV) – All new cars sold in California starting in 2004 will have at least a LEV or better emissions rating.

2. Ultra Low-Emission Vehicles (ULEV) – Cars that are 50% cleaner than the average new 2003 model year car receive an ULEV emissions rating.

3. Super Ultra Low-Emission Vehicle (SULEV) – Cars that are 90% cleaner than the average new 2003 model year car receive a SULEV emissions rating.

4. Partial Zero Emission Vehicle (PZEV) – Cars that meet the SULEV emission standards, have zero evaporative emissions, and have a 15 year/150,000 mile warranty on emissions equipment, will receive a PZEV emissions rating.

5. Advanced Technology PZEV (AT PZEV) – Cars that meet the PZEV requirements and have additional "ZEV-like" characteristics receive an AT PZEV emissions rating. A dedicated compressed natural gas vehicle, or a hybrid vehicle with engine emissions that meet the PZEV standards, would have an AT PZEV rating.

6. Zero Emission Vehicles (ZEV) – These cars have zero tailpipe emissions and are 98% cleaner than the average 2003 model year vehicle. Examples include the battery electric vehicle and hydrogen fuel cell vehicles.

OTHER STATES' INFORMATION

The states surveyed include *Florida*, *Illinois*, *Massachusetts*, *Michigan*, *Minnesota*, and *New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws. Research found that a hybrid vehicle deduction or tax credit is unavailable in these states under current law.

FISCAL IMPACT

The department's costs to administer this bill are indeterminable until implementation concerns have been resolved, but are anticipated to be minor after resolution of those concerns.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

This bill fails to specify both the percentage of costs that would qualify for the credit and how the actual credit base ("aggregate amount paid") would be determined, and also has other undefined terms, thus it is impossible to determine what the revenue impact is at this time.

POLICY CONCERNS

This bill fails to limit the number of years for the carryover period. The department would be required to retain the carryover on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation because experience shows credits typically are exhausted within eight years of being earned.

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of tax credits by the Legislature.

This bill would allow taxpayers in certain circumstances to claim multiple tax benefits, namely the hybrid vehicle credit and the depreciation deduction, for the same item of expense. The author may want to require that the depreciable basis of the qualified vehicle be reduced by the amount of the hybrid vehicle credit.

A hybrid vehicle may qualify for the state's credit, but fail to qualify for the federal tax credit. Federal law has differing rules such as when sales of hybrid cars reach a certain amount. This may cause confusion for taxpayers.

If a taxpayer pays for a car purchase or lease over time, the taxpayer would get a credit for only the amount of installment payments made during the taxable year.

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